

that is fairly attributable to improvements made by them after purchase.

(b) *Promissory note method.* Where there is potential for a windfall profit because the dwelling unit is sold to the initial purchaser for less than fair market value, without a commensurate limited or shared equity restriction, the initial purchaser shall execute a promissory note, payable to the PHA, along with a mortgage securing the obligation of the note, on the following terms and conditions:

(1) The principal amount of indebtedness shall be the lesser of:

(i) The purchase price discount, as determined by the definition in paragraph (a) of this section and stated in the note as a dollar amount; or

(ii) The net resale profit, in an amount to be determined upon resale by a formula stated in the note. That formula shall define net resale profit as the amount by which the gross resale price exceeds the sum of:

(A) The discounted purchase price;

(B) Reasonable sale costs charged to the initial purchaser upon resale; and

(C) Any increase in the value of the property that is attributable to improvements paid for or performed by the initial purchaser during tenure as a homeowner.

(2) At the option of the PHA, the note may provide for automatic reduction of the principal amount over a specified period of ownership while the property is used as the purchaser's family residence, resulting in total forgiveness of the indebtedness over a period of not less than five years from the date of conveyance, in annual increments of not more than 20 percent. This does not require a PHA's plan to provide for any such reduction at all, or preclude it from specifying terms that are less generous to the purchaser than those stated in the foregoing sentence.

(3) To preclude collusive resale that would circumvent the intent of this section, the PHA shall (by an appropriate form of title restriction) condition the initial purchaser's right to resell upon approval by the PHA, to be based solely on the PHA's determination that the resale price represents fair market value or a lesser amount that will result in payment to the PHA, under the note, of the full

amount of the purchase price discount (subject to any accrued reduction, if provided for by the homeownership plan pursuant to paragraph (b)(2) of this section). If so determined, the PHA shall be obligated to approve the resale.

(4) The PHA may, in its sole discretion, agree to subordination of the mortgage that secures the promissory note, in favor of an additional lien granted by the purchaser as security for a loan for home improvements or other purposes approved by the PHA.

(c) *Limited equity method.* As a second option, the requirement of this section may be satisfied by an appropriate form of limited equity arrangement, restricting the amount of net resale profit that may be realized by the seller (the initial purchaser and successive purchasers over a period prescribed by the homeownership plan) to the sum of:

(1) The seller's paid-in equity;

(2) The portion of the resale proceeds attributable to any improvements paid for or performed by the seller during homeownership tenure; and

(3) An allowance for a portion of the property's appreciation in value during homeownership tenure, calculated by a fair and reasonable method specified in the homeownership plan (e.g., according to a price index factor or other measure).

(d) *Third option.* The requirements of this section may be satisfied by any other fair and reasonable arrangement that will accomplish the essential purposes stated in paragraph (a) of this section.

(e) *Appraisal.* Determinations of fair market value under this section shall be made on the basis of appraisal within a reasonable time prior to sale by an independent appraiser, to be selected by the PHA.

§ 906.15 Use of sale proceeds.

(a) *General authority for use.* Sale proceeds may, after provision for sale and administrative costs that are necessary and reasonable for carrying out the homeownership plan, be retained by the PHA and used for housing assistance to low-income families (as such families are defined under the Act). The term "sale proceeds" includes all

payments made by purchasers for credit to the purchase price (e.g., earnest money, downpayments, payments out of the proceeds of mortgage loans, and principal and interest payments under purchase-money mortgages), along with any amounts payable upon resale under § 906.14, and interest earned on all such receipts. (Residual receipts, as defined in the ACC, shall not be treated as sale proceeds.)

(b) *Permissible uses.* Sale proceeds may be used for any one or more of the following forms of housing assistance for low-income families, at the discretion of the PHA and as stated in the HUD-approved homeownership plan:

(1) In connection with the homeownership plan from which the funds are derived, for purposes that are justified to ensure the success of the plan and to protect the interests of the homeowners, the PHA and any other entity with responsibility for carrying out the plan. Nonexclusive examples include nonroutine maintenance reserves under § 906.11; a reserve for loans to homeowners to prevent or cure default or for other emergency housing needs; a reserve for any contingent liabilities of the PHA under the homeownership plan (such as PHA guaranty of mortgage loans); and a reserve for PHA repurchase, repair and resale of homes in the event of defaults.

(2) In connection with another HUD-approved homeownership plan under this part, for assistance to purchasers and for reasonable planning and implementation costs.

(3) In connection with a State or local homeownership program for low-income families, as described in the homeownership plan, for assistance to purchasers and for reasonable planning and implementation costs. Under such programs, sales proceeds may be used to construct or acquire additional dwellings for sale to low-income families, or to assist such families in purchasing other dwellings from public or private owners.

(4) In connection with the PHA's other public housing that remains under ACC, for any purposes authorized for the use of operating funds under the ACC and applicable provisions of the Act and Federal regulations, as included in the HUD-approved operating

budgets. Examples include maintenance and modernization, augmentation of operating reserves, protective services, and resident services. Such use shall not result in the reduction of the operating subsidy otherwise payable to the PHA under 24 CFR part 990.

(5) In connection with any other type of Federal, State, or local housing program for low-income families, as described in the homeownership plan.

§ 906.16 Replacement housing.

(a) *Replacement requirement.* As a condition for transfer of ownership under a HUD-approved homeownership plan, the PHA must obtain a funding commitment, from HUD or another source, for the replacement of each of the dwellings to be sold under the plan. Replacement housing may be provided by one or any combination of the following methods:

(1) Development by the PHA of additional public housing under 24 CFR part 941 (by new construction or acquisition).

(2) Rehabilitation of vacant public housing owned by the PHA.

(3) Use of five-year, tenant-based certificate or voucher assistance under Section 8 of the Act.

(4) If the homeownership plan is submitted by the PHA for sale to residents through an RMC, resident organization or cooperative association which is otherwise eligible to participate under this part, acquisition of nonpublicly-owned housing units, which the RMC, resident organization or cooperative association will operate as rental housing, comparable to public housing as to term of assistance, housing standards, eligibility, and contribution to rent.

(5) Any other Federal, State, or local housing program that is comparable, as to housing standards, eligibility and contribution to rent, to the programs referred to in paragraphs (a)(1) through (a)(3) of this section, and provides a term of assistance of not less than five years.

(b) *Funding commitments.* Although a HUD funding commitment is required if the replacement housing requirement is to be satisfied through any of the HUD programs listed in paragraph (a) of this section, HUD's approval of a Section 5(h) homeownership plan on